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NEW APPROACHES TO SALVAGING THE SOCIAL SECURITY PROGRAM

ORIGINAL

HEARING

BEFORE THE

SUBCOMMITTEE ON MONETARY AND FISCAL POLICY

OF THE

JOINT ECONOMIC COMMITTEE

CONGRESS OF THE UNITED STATES

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NEW APPROACHES TO SALVAGING THE SOCIAL SECURITY PROGRAM

TUESDAY, JULY 27, 1982

CONGRESS OF THE UNITED STATES,
SUBCOMMITTEE ON MONETARY AND FISCAL POLICY
OF THE JOINT ECONOMIC COMMITTEE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 2 p.m., in room 6226, Dirksen Senate Office Building, Hon. Roger W. Jepsen (chairman of the subcommittee) presiding.

Present: Senator Jepsen.

Also present: James K. Galbraith, executive director; and Mark R. Policinski, Chuck Ludlum, and Richard Vedder, professional staff members.

OPENING STATEMENT OF SENATOR JEPSEN, CHAIRMAN

Senator JEPSEN. The Subcommittee on Monetary and Fiscal Policy of the Joint Economic Committee will come to order.

Two of America's more pressing problems are the sluggish growth in productivity and the growing crisis in the social security system. We need to increase investment in this country by making more funds available at lower interest rates. We need to reevaluate our social security system with the hope of restoring faith and confidence in it by putting it on a sound footing.

Today we are pleased to have with us my very good friend from Bettendorf, Iowa, Dr. Donald Hansen, who will offer us an idea on how we might reform our social security system, stimulating the economy as well.

I am pleased to welcome you, Don, and look forward to your testimony.

STATEMENT OF DONALD H. HANSEN, DOCTOR OF OPTOMETRY, BETTENDORF, IOWA

Dr. HANSEN. Thank you, Mr. Chairman.

The present system is failing Americans. It did not account for an increase in the number of older Americans, a declining birth rate, high rates, and stagflation.

It is doubtful that adequate social security funds will be available for working Americans who pay enormous amounts of social security taxes and may be looking at retirement in as few as 10 years.

This proposal is an alternative to our present system with a prepaid investment that accrues interest that guarantees every American a retirement income.

The fund is invested at birth in a trust fund for every American. With compounding interest the individual can retire with a healthy income and never pay social security taxes.

The concept of prepaid social security is a unique approach for restoring the present social security program in the United States, but it is one that should be considered in these challenging times, and it is feasible in our free enterprise economy. If properly designed and implemented, such a plan could revitalize our Nation.

This plan could phase out social security taxes, in turn, increase the social security benefits, revitalize the homebuilding and farm machinery industries, and with lower mortgage and bank loan interest rates, reduce inflation; in turn, reduce crime.

It would lead to earlier retirement, thereby creating more jobs. Above all, this plan would be easily understood, and something we all could believe in.

I believe that all this is possible because of America's inherent financial strength and the American people's willingness to commit that strength toward goals for social, financial, and civil security.

We need in America today low-interest loans to extinguish the flames of inflation. The reward for this lessened demand is reduced inflation, lower interest loans, more jobs, new homes, and new farm machinery. As President Kennedy said, "A rising tide lifts all boats."

Backed and supported by the American people are national assets. A stable and guaranteed social security system can provide a solid base to insure our Nation's economic growth.

Let us speculate on what such a premise might mean. In 1979 there were 3,483,000 births in the United States. Had the program been in force, a total of $3,483 million would have poured into our social security fund. These funds could provide a source for bankers to obtain long-term money for new houses and farm machinery.

Banks are presently struggling because they have outstanding long-term low-interest loans and are presently losing money on them. Consequently, they have to raise the present short-term notes to survive. It could help to fight inflation and revitalize all our industries and create new jobs. Any competition in the interest market would tend to lower the general interest rates and lower inflation.

My solution would be to have high employment, which I believe is the best solution to our present system.

We need 3 million to 4 million new jobs today. The financial boost to the economy would shore up the present social security system by creating more jobs paying into it.

Under the prepaid social security system, once a newborn has been funded with $1,000 deposit into a personal account, he or she will never have to pay social security taxes. The employer's expense of computing, deducting, and paying social security taxes would be eliminated, thus reducing overhead and increasing profits.

By having optional retirement after age 60, more jobs would open up, giving a greater boost to our national economy. For example, a husband and wife could retire at age 60 with $608,000 in their combined personal trust fund, or more than $2,000 a month for 25 years.

Before retirement their trust fund could be used for borrowing a down payment on a home, for college or vocational education. Payments could be deducted automatically from the individual's account, thus reducing the percentage of our taxes assigned to support Federal health care programs such as medicaid and medicare.

By using the national mortality rate, we reassign money back into the fund. If a person dies before reaching retirement age, the initial $1,000 and its earnings are paid out—are not paid to his or her estate, but instead revert back into the social security system.

Exceptions to this would occur in the awarding of benefits to the surviving spouse and children. I believe this plan could be easily taught in our educational system—the funded children would feel personal pride in the country's and their own personal economic achievement. There would be a new involvement and awareness of business.

In addition, by controlling the purse strings on an individual's trust fund, society would have an added way to discourage crime. For the first time criminals who have been capitalized under the system would have to pay for their transgressions out of their trust fund, reimbursing victims for their losses and reducing the taxpayers' obligations to support the criminal justice system.

Again, for the first time, the United States would have a certain measure of control to accelerate or decelerate economic growth. This unique free enterprise ability would come about without any deficit financing or taxation.

There are two great sources of funds in the United States: One is the social security fund, and the other is our defense fund. We are obviously only looking at our social security fund to work with when considering economic growth.

If we added the births in 1976 through 1980, and subtracted the mortality rate, we could assume approximately $20 billion in fresh social security funds.

This amount of money would be available on a 5-year basis for 10-percent loans to finance new homes, farm equipment, and factory retooling. This would mean new jobs, increased sales, and production. Above all, it would mean hope for the future.

Do you have any comments at this point?

Senator JEPSEN. Thank you, Dr. Hansen.

In your plan, Doctor, who is going to provide the funds for the $1,000 grant or loan to each American at birth? Is that coming from general revenues or from a new tax?

Dr. HANSEN. The initial loans would be coming from general revenues. We have done a computer study on this. If all of the money that accrued through mortality rates went back into the funds, at the end of 20 years we would have a profit of $11.5 billion. If we started refunding the system from itself or recycling the funds back, we could do this in about 4 to 5 years. We would have a self-sustaining fund.

You must remember that in about 20 years when these funded children grow up and marry and start having children, they have funds which could automatically fund their offspring, so the Government would be out of the business in as few as 5 and as late as 20 years, depending on how you wanted to do it.

Senator JEPSEN. If they were to fund their offspring, would they borrow then from their own established fund to loan another $1,000

for their offspring or how would that work? Where would that come from?

Dr. HANSEN. They would automatically fund their own offspring out of each fund. The mother would take $500 and the father would take $500 and it would be an automatic procedure. Or they could simply pay the money; they don't have to borrow from their funds.

In the beginning, of course, it has been estimated that not everybody would contribute to pay off their loan; we anticipate that case for approximately 60 percent of the people. If the parents can afford to pay the loan, they would do so and have $1,000 deduction on their income tax. If they were abandoned babies and had no one to pay their loan off, this loan would be at 8 percent and at 2 percent interest. This would give them an incentive as they grew up to see how the system works. By adding more to their account, they would have greater funds in retirement.

Senator JEPSEN. Would your system apply only to newly born Americans or would it apply to all Americans, or to Americans who have not begun payments to our existing system?

Dr. HANSEN. I would anticipate that if this plan were inaugurated, that it would apply to all Americans. It would be like in addition to paying social security taxes, as we all do now, there would be an individual social security IRA fund that would be part of your estate. And you could contribute whatever you wished, so the funds on that have not even been calculated.

Everybody would each have an IRA account along with their social security account.

Senator JEPSEN. Who would run your system? Would there be substantial administrative problems or additional personnel needed, or could you do it within the present structure?

Dr. HANSEN. I anticipate, since it is a social security solution, that the Social Security Administration would run it. In this, if we start a new system, we have an excellent opportunity for the first time to incorporate in it something I think is lacking in a lot of our Government transactions and things, and that is to have a service charge.

If you wanted to borrow from your fund, which might be upward to $30,000 or $40,000, as this money accumulates to borrow money for a house, there might be a $100 payment or something to the system to pay for the effort involved in getting your money out and making the down payment. And if we put this on a self-sustaining basis it could pay its own way.

I would like to see America recycle its money for its own good. If you take $1 in over 60 years and apply 10-percent interest it becomes $300, and by getting this to the school system and teaching children that—and parents and grandparents that can contribute to this fund, I think we can go a long way toward solving some of our problems.

Senator JEPSEN. You assume a 10-percent interest rate as a return on the investment funds. Historically, real interest rates; that is, return on funds after we account for inflation have been far less than that.

The likelihood, if we were talking about getting our economy moving and so on, is that real interest rates projected out in the future for half a century or another century would be considerably less than that.

What is your reaction to this?

Dr. HANSEN. I don't think we are going back to the 2-, 3-, or 4-percent interest that we have had in years past. I think with the demand for money for Third World development and space exploration that 10 percent is a realistic figure to talk about.

I hope that they come down from the 15- to 16-percent level, but certainly the 10-percent level—it could be 8, 9, or 11, but we're using 10 percent as a conversation piece. When you consider a loan—to gear this to inflation, I have a moratorium—I use a 10-percent figure for 5 years, and after the 5 years' date loan, the interest rate is adjusted to the inflation rate.

If you have, for example, a 10-percent loan and 10-percent inflation, at the end of 60 years you have nothing. In order to put a cap on inflation, I have offered to bring to the interest market some competition that it has never had before.

And the competition would exist in a system where all American people are contributing, and this contribution would consist of putting their $1,000 in for all of the funded children and for 5 years it would be at a lower rate of interest than the current market.

Now it is possible interest rates could drop, but any loans after that—for example, after 5 years—would have to be accountable to adjust for the inflation rate. They go into effect for 5 years and after that they go to whatever the rate of inflation—if we have a 10-percent loan, after 5 years there is 5-percent inflation, then the new note becomes 15 percent.

Now, that sounds high. But when you consider that you are not paying any social security taxes for one, and two, you are paying part of that to yourself, it is a reasonable figure.

Senator JEPSEN. Your plan, I heard you say, would not have any social security taxes whatsoever, so that there would be an immediate tax relief for everyone in this country. How would the transition work with the Americans who are presently under social security?

Dr. HANSEN. I think we are going to have to keep our present system and pay the benefits that we have obligated ourselves to. I would not change that at all.

They have come to expect these things, and we should leave well enough alone.

Senator JEPSEN. Your system would apply only to newly born Americans?

Dr. HANSEN. Yes; to start with. My system would also, hopefully, by recycling money, stimulate growth, and create jobs, and these people would then pay into our present system—the new jobs, people going back to work again are going to stay under the same system for a while, and they would by having new jobs pay into the present system.

Senator JEPSEN. What do the social security system people think of this prepaid proposal? Have you discussed it with any of them?

Dr. HANSEN. I have had a preliminary discussion with them, and it is my understanding that this plan, along with five or six others they are considering, would be reviewed. I believe they are having a meeting later in August.

Senator JEPSEN. I am aware of the extensive time, effort, and research that you personally put in this, and the expense that you have gone to to have others assist you with it.

During this research, have you looked into the experience of Chile, which is moving in the direction that this system you are advocating is going? Have you happened to run across that?

Dr. HANSEN. Would you repeat that?

Senator JEPSEN. Have you looked into the experience of Chile, which has moved a step in the direction of the system you are advocating? Are you familiar with it?

Dr. HANSEN. The country of Chile has recently inaugurated in the last several years a new system that incorporates something along this line, where they are recycling money to build apartment houses and things that they need in their country.

They have gone one step further in a certain direction; they have established official investment groups where a person has the option of joining his or her account with this group or that group. And there are maybe five or six that are accredited by the Government of Chile, and they supervise these accounts. You can change from one governing group to another. It is a system that I am not totally familiar with, but it is one of the more modern ones that they are experimenting with, and they are in effect recycling money.

Senator JEPSEN. Does the prepaid system that you are advocating—and I understand you have more detailed analysis of this and programing of it available—suggest any strengthening or reinforcement of the present system?

Do you have any recommendations for changing the present system at all to make sure it does what it has promised it is going to do over the years?

Dr. HANSEN. From all of the proposals I have read, I understand that there are about three things they are thinking about doing with the present system, and there may be more that I don't know about.

The three are—they are thinking about having people work until 67; they are thinking about borrowing from other funds in the system, or they are taking money from the general treasury.

I do not think that is the answer at all. I think that is wrong, and I think the real answer is to come up with a system—mine or somebody else's—that creates jobs. We desperately need jobs. I forget how many homes were foreclosed in the last 30 days in this country. There is a desperate need for people to have some hope, and we need to develop a system that recycles money toward ourselves and build a sounder system.

I think by doing so we are going to create jobs. There are a lot of companies who aren't afraid to expand; they cannot afford it. If we could offer them a large amount of money that would be at a lower rate of interest that would be backed by our social security system, it would have broad implications in our nation. It would have broad international implications because of the stability of our country.

We are the greatest doers in the world, and if ever we had an opportunity in this world to show the world how free enterprise can do something, this is our chance. We should not have a failing system; we have great economists and money managers—leaders—in this country. We have a system we're almost ashamed of; and I feel we should come up with something that is a little bit practical or innovative—a little excitement to it—that can lift our hope. We need to give people hope.

Senator JEPSEN. You're certainly on target there, Doctor. Two of America's most pressing problems are our sluggish economy and the grand crisis that we have in our social security system. So the need to reevaluate the social security system is one that you recognized early on some 2 years ago and have spent a great deal of time and research and effort to develop and, as you have proposed here today, to substitute a prepaid system for our present system.

We, in addition to that, have the additional challenge here in the Congress of restoring faith and confidence. And the one we have—even if we put in the prepaid system—to make sure that it does fulfill the promises that have been made throughout the years—our Government has made to the participants in the present social security system.

So I do thank you for not only your interest, but for all the work that you have put in. It is only through public-spirited citizens like you that a democracy really does operate and work effectively. Because we do derive our power and also our ideas and our creativity from the bottom up in this country and not from the top down.

So the Senate is indebted to you and I thank you. Do you have any closing statement you would like to make?

Dr. HANSEN. No, I th nk I have pretty well summarized my feelings. I do want to thank you again for the time and opportunity to make this presentation.

I think it speaks highly of the system that allows someone to come in who is not an official professional in the field of economics to present a plan that I think is a practical solution, and a simple solution—one that can be in our school system; and as you know, in our school system today, beginning in the third and fourth grade, the bank officials are coming in and teaching children how to have a checking account and balance checkbooks and so forth.

And under this plan everybody would have an annual receipt or ticket they would get in the mail from their social security showing how much money they had. And they could watch their money grow.

And I think this would be very inspiring to people who maybe do not have anything in the world to know that their country loves them; that the country believes in them, and is going to give everyone the same chance for equality.

Senator JEPSEN. Thank you very much. The subcommittee is adjourned.

[Whereupon, at 3:08 p.m., the subcommittee adjourned, subject to the call for the Chair.]

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